# Federal Taxation of Admissions to Athletic Contests of State Universities

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The Federal Revenue Act of 1932 Sec. 711 (a) amends the Act of 1926 Sec. 500 (a) so as to impose "a tax of 1c for each 10c or fraction thereof of the amount paid for admission to any place, including admissions by season tickets or subscriptions, to be paid by the person for such admission; except that in case the amount paid for admission is less than 40c, no tax shall be imposed."

The Act of 1926 Sec. 500 (b) (1) provides an exemption from the payment of taxes levied on admissions, the proceeds of which inure exclusively to the benefit of educational institutions. The Act of 1932 amends this provision Sec. 711 (c) and reads, "The exemption from tax provided by subdivision (b)(1) shall not be allowed in the case of admissions to any athletic game or exhibition, the proceeds of which inure wholly or partly to the benefit of any college or university (including any academy of the military or naval forces of the United States)."

The statute, according to these provisions, makes no exception for any State school, college, or university, so that the purchaser of an admission must pay a Federal tax on such admissions to athletic contests though they be conducted by State educational institutions on their own property and for their own benefit.

The problem at once arises as to whether or not such a tax is unconstitutional, first as being a tax which operates to burden an instrumentality or agency of the State, and secondly as being a burden on the officers and employees of the State by placing upon them duties in respect to the administration of Federal laws and the collections of Federal taxes.

It is valuable as a back ground that we notice the present status of this Act relative to State educational institutions over the country. Practically all of these institutions are collecting such tax and paying it over under protest to the Federal Government; Ohio State University is doing this.

It is interesting to observe that if the statute under consideration is declared unconstitutional as applied to State schools, the amount so paid-in could not be clamed by the institutions themselves, but only by those individuals who purchased tickets and who paid the tax, upon due proof of such facts.

The University of Iowa at Iowa City has collected the tax and impounded it, but the State College at Ames has refused to collect it in the first instance. The action of these institutions was taken as the result of an opinion by Neill Garrett, Assistant Attorney General of the State of Iowa, contained in a letter of September 15, 1932, addressed to the University of Iowa. The decision in such letter was that the tax was a burden upon the State in its performance of an essential governmental function.[1]

The University of Minnesota at Minneapolis has collected the tax and impounded it following an opinion of Henry N. Benson, Attorney General of the State of Minnesota, rendered in a letter of September 23, 1932, addressed to the Comptroller of the University of Minnesota. The Federal Act was declared unconstitutional because first, it burdened the State in its carrying out a governmental function, and secondly, it burdened officers of the State with duties in respect to administering Federal laws and collecting Federal taxes.[2]

[1] In the letter Mr. Garrett said, "The question arises at once as to whether or not the Federal Government has the power to thus burden an agency or instrumentality of the State Government, such as State colleges and universities which are absolutely State supported and which are controlled by the legislature of the State and the State Board of Education, which is a creature of the State law and draws its very life, sustenance and authority from the provisions of State law.

"We shall not undertake to set out or to review herein the various decisions of higher courts relative to the principle involved in this matter. It is sufficient to say that a State College or University is an instrumentality of the State engaged in performing a strictly governmental function.

"It is suggested that the Federal tax on admissions involved herein is expressly levied on the 'person paying such admission' so that no burden is imposed upon the state institution, it being merely a collecting agency. This, however, does not avoid the difficulty nor answer the question. The courts have held that the Federal government cannot burden, even to a slight degree, a strictly governmental function of the State government, and that if such a thing would be permitted, there would be a tendency toward impairment of governmental agencies under State control. Also, the charging of admissions to athletic contests is a means employed by the college and university regents and boards, and in the case of State institutions, by the State, for raising revenue for the purpose of defraying at least a part of the expense of conducting the physical education programs, and, therefore any Federal tax imposed upon that means necessarily burdens the States in its conduct of such a governmental enterprise.

"Hence it seems clear to us that the Federal tax herein referred to is an interference with and a burden upon a governmental function of the State."

[2] Mr. Benson's letter reads, "The Supreme Court of this State has held in effect that the University is a 'Constitutional Corporation' and as such is an agency of the State government to accomplish a State purpose: *George* v. *University*, etc., Association, 107 Minn. 424; State ex. rel. *Smith* v. *Reed*, 125 Minn. 194; State ex. rel. *University* v. *Chase*, 175 Minn. 295. It is our understanding that the athletic games and exhibitions conducted by the university and participated in by students thereof augment the funds available to the Board of Regents for the maintenance of the university, and that substantial net profits accrue from these games and are used for general university purposes.

"Since the University is an agency of the State and is engaged in the performance of a State function, it follows that the games and exhibitions in question are proper governmental activities of the State. This being established, it follows that within the docrine of *Gillespie* v. *Oklahoma*, 257 U.S. 501, and *Burnett* v. *Coronado Oil Co.*, 285 U.S. 393, and other decisions of the U. S. Supreme Court therein cited, a tax upon admissions to

In West Virginia there is a suit now pending in the Federal Court for the Northern District of West Virginia which will be heard at the Elkins, June, 1935, Term of Court.

This suit involves the University of West Virginia at Morgantown, but, because of the peculiar factual situation, such may not serve as a fair test of the problem before us. During the season following the passage of this Federal Revenue Act of 1932 the tickets of the university were itemized as $1.00 for admission and 10 cents for Federal tax. The Federal government does not seek to recover for a failure to levy and collect the tax in the past, nor to compel a levy and collection in futuro, but brings suit to recover only such amounts as was levied and collected under the tickets which carried the itemization of the 10c Federal tax. The Athletic Department segregated the admission and the tax items on the tickets, but when the proceeds were received, they recorded them as lump sum proceeds without any corresponding demarcation, and failed to turn the tax item in to the Federal government. The Department now prints the tickets at a lump sum price without any itemization of a Federal tax.

The case does not appear very favorable in so far as the University of West Virginia is concerned, for even if the court assumes the Federal act to be unconstitutional upon either of the two grounds which we have enumerated as being the basis of the discussion at hand, it does not seem that the State could claim the proceeds as against the Federal government.

The tax has been collected for the Federal government. If the

those games and exhibitions is in effect a tax upon a governmental function of the State, and in our opinion, may not lawfully be imposed by the Federal Government.

"Under the terms of the revenue act it is made the duty of every person receiving payments for admissions subject to this tax to collect the amount thereof from the person making such payments. Return under oath must be made concerning the taxes so collected to the collector of the proper district, and the moneys so collected paid at the time the same are due. The commissioner of internal revenue, in accordance with the terms of the act, has prescribed regulations in respect to keeping daily records of all classes of admissions, and these records shall be available to inspection by the U. S. authorities. In order to comply with the act and with these regulations a person receiving payment of the admissions tax must necessarily be subjected to considerable additional responsibility and trouble in the matter of keeping the records prescribed in the manner required. We think it is well established by the decisions that the Federal government may not lawfully burden officers and employees of a state with duties in respect to the admission of the federal laws and the collection of federal taxes. It is likewise true that the State cannot impose duties relating to its own governmental functions upon officers or employees of the Federal government. It occurs to us, therefore, that in attempting to make it the duty of the State to collect, keep record of, and remit to the Federal government an admission tax upon games and exhibitions given by a state university which occupies the status of the University of Minnesota, Congress has exceeded its powers, and that the State cannot thus be compelled to act as an agency of the Federal government.

"It is therefore our opinion that the tax on admissions as prescribed by the Federal Act is not applicable to payments made by persons for admission to athletic games and exhibitions of the University of Minnesota."

Federal act is unconstitutional as being a burden upon an instrumentality by which the State exercises an essential governmental function, the Athletic department could not claim the tax so collected as its own. Such would belong to those individuals who paid the tax, upon their duly proving such fact, but the contest for the proceeds would always be between those individuals and the Federal government who was responsible for the tax and for whom it was collected by the State. The State might intervene in the litigation to aid in having the act declared unconstitutional, yet there would still remain the necessity of those individuals who paid the tax proving they had done so, before the Federal government would be required to refund the amount to them.

On the other hand if the act was to be declared unconstitutional for placing duties of enforcing Federal acts upon officers of the State, there is the fact that there was no express prohibition by the State against their collecting such tax. A State can consent to its officers performing certain functions for the Federal government; it seems that the complaint should come before and not after the duty has been performed to the knowledge of the State. The contest for the proceeds would likewise be between the individuals who paid the tax and the Federal government.

It is noticeable that neither any State nor the Federal government wishes to take the initial step in the litigation, both realizing that the issue is a close one and neither wishing to be the aggressor unless there are certain factors involved which lends strength to their side. But when we observe on the part of the Federal government the enormous, steadily mounting public debt necessitating the tapping of every available source of income, while on the part of State institutions their curtailed budgets, fixed debt, and fall-off in attendance it is seen that the acuteness of the situation may lead to actual litigation in the near future.

## Federal Taxation as a Burden on an Agency or Instrumentality of the State.

### A. *The General Rule and Its Application.*

The first decision of the Supreme Court of the United States bearing upon the now established rule of the freedom of instrumentalities, means, and operations of the Federal and State governments in exercising their governmental functions, from taxation by its co-sovereign, was rendered by Chief Justice Marshall in the famous case of *McCullough* v. *Maryland*, 4 Wheat. 316, 4 L.E. 579 (1819).

The converse of this rule, i.e., that the Federal government cannot tax the instrumentalities of the State government in carrying out its gov-

ernmental functions, was established in *Collector* v. *Day*, 11 Wal. 113, 20 L.E. 122 (1870), wherein the court declared that it was not competent for Congress to impose a tax upon the salary of a judicial officer of the State. The reasoning in this case was identical to that of the McCullough case, that of protecting the independence of the two governments in their respective fields.

As the rule was applied to different facts in subsequent cases, the courts early recognized that each extension of immunity to one government involved as a correlate, a curtailment of the taxing power of the other, which power was as essential to the one levying the tax as it was to the one claiming the immunity. The first clear statement was made in *R. R. Co.* v. *Peniston*, 18 Wal. 5, 21 L.E. 787 (1878), wherein the opinion reads, "It can't be said that every State tax which remotely affects the efficient exercise of a Federal power is for that reason alone inhibited by the Constitution. To hold that would be ot deny to the State all power to tax persons and property. Every tax levied by a State withdraws from the reach of Federal taxation a portion of the property from which it is taken, and to that extent diminishes the subject upon which the Federal tax may be laid. The States are, and they must ever be, coexistent with the National government. Hence the Federal Constitution must receive a practical construction. Its limitations and its implied prohibitions must not be extended so far as to destroy the necessary powers of the State, or prevent their effective exercise."

We are then able to see the problem in the light of the rule and its qualification. If the tax of one sovereignty operates directly to burden an instrumentality of its co-sovereign in its exercise of a governmental function, such tax is unconstitutional and void. But whether the tax is or is not a burden must be considered from an angle of practicability by the courts, with a realization that not every tax which can, in some indirect manner be shown to burden a State or the Federal government if one of its functions should be declared void, since an extension of immunity to one involves a curtailment of power in the other.

However, this issue of practicability in its turn has a qualification. If the instrumentality is one by which either of the sovereigns exercises an essential governmental power directly, any tax thereupon is a direct burden and unconstitutional without regard to the amount of the particular tax or the extent of the resulting interference. Where the immunity exists it is absolute, resting on the entire absence of power to tax even slightly, because this power to tax involves a potential power to destroy entirely. *McCullough* v. *Maryland*, supra; *U.S.* v. *B. and O. R. R.*, 17 Wall 322, 21 L.E. 587 (1872); *Johnson* v. *Maryland*,

254 U. S. 51, 41 S.C. 16 (1920); *Gillespie* v. *Oklahoma*, 257 U. S. 501, 42 S.Ct. 171 (1922); *Indian Motorcycle Co.* v. *U. S.*, 283 U. S. 570, 51 S.Ct. 601 (1931).

On the other hand it is apparent that not every person who uses his property or derives a profit in dealing with a State or the Federal government can claim an immunity from taxation on the theory of being an instrumentality of that government within the meaning of the rule. The courts have refused to grant such immunity when there is no direct burden laid upon a governmental instrumentality, and there is only a remote, if any, influence upon the exercise of the function of government. *Baltimore Shipping Co.* v. *Baltimore*, 195 U. S. 375, 25 S.Ct. 50 (1904); *Gromer v. Standard Dredging Co.*, 224 U. S. 362, 32 S.Ct. 499 (1912); *Metcalf and Eddy* v. *Mitchell*, 269 U. S. 514, 46 S.Ct. 172 (1926); *Education Film Co.* v. *Ward*, 282 U. S. 379, S.Ct. 170 (1931); *Burnett* v. *A. T. Jergins Trust Co*, 288 U. S. 508, 53 S.Ct. 439 (1933); *Trinityfarm Co.* v. *Grosjean*, 291 U. S. 466, 54 S.Ct. 469 (1934).

Quoting from *Metcalf and Eddy* v. *Mitchell*, supra, "As cases arise between these two extremes it becomes necessary to draw the line which separates the activities having some relation to the government, which are nevertheleess subject to taxation, from those which are immune. Experience has shown that there is no formula by which the line may be plotted with precision in advance. But recourse may be had to the reason upon which the rule rests, and which must be the guiding principle to control its operations. Its origin was due to the essential requirement of our Constitutional system that the Federal government must exercise its authority within the territorial limits of the state; and it rests on the conviction that each government, in order that it may administer its affairs within its own sphere, must be left free from undue influence by the other."

*S. Carolina* v. *U. S.*, 199 U. S. 437, 26 S.Ct. 110 (1905), added one further qualification to the general rule which must not be overlooked. In that case the State of S. Carolina, through its own officers and agencies, carried on the liquor business. The court held that the income therefrom was not exempt from the Federal Internal Revenue Act; that when a State engages in a business of a private nature, such business is not thereby withdrawn from the taxing power of the Federal government. This same case was cited with favor in *Flint* v. *The Stone-Tracy Co.*, 220 U. S. 107, 31 S.Ct. 342 (1911) wherein the conclusion was made that it was no part of the essential governmental functions of a State to provide means of transportation, supply artificial

light, water, and the like; also that "the exemption of State agencies and instrumentalities from national taxation is limited to those of a strictly governmental character, and does not extend to those used by the State in carrying on a business of a private nature. See also *Ohio* v. *Helvering*, 292 U. S. 360, 54 S.Ct. 725 (1934); *Helvering* v. *Powers*, 293 U. S. 214, 55 S.Ct. 171 (1934). In these cases the court is concerned as to the type of function which is being carried on; whether or not such is an essential governmental function. If it is not then the activity is not exempt from taxation by the co-sovereign, and the fact that the medium is an agency or instrumentality of the State or Federal government is of no importance.

With this general rule in mind it will aid us in our consideration of this problem, to observe the decisions of the courts in an effort to discover where this line is drawn which separates the exempt from the non-exempt. For convenience and clarity the cases have been grouped into two main sections with subdivisions thereunder; such arrangement making possible a comparison of substantially similar situations as well as aiding us in determining into which factual situation or situations the circumstances of our case takes us.

The first section is that of taxation upon property where the tax is levied primarily for the purpose of revenue to the taxing government. A State cannot tax real property within its borders while owned by the United States as proprietor, to be used for arsenals, fortifications, court houses, and the like. *Van Brocklin* v. *Tenn.*, 117 U. S. 151, 6 S.Ct. 670 (1886). But a State can tax real property of a railroad corporation deriving its existence from Federal law, exercising its franchise under such law, and holding property within the State; and this is so although the railroad is engaged in service for the United States government. *Thompson* v. *U. P. R. R.*, 19 Wal. 579, 19 L.E. 792 (1869). In this railroad situation it seems that the State could not however levy and collect a tax upon the operation of a railroad, since such would be a direct obstruction to the exercise of Federal powers within the instrumentalities rule. *R. R.* v. *Peniston*, supra. Again in *Western Union Telegraph Co.* v. *Mo.*, 190 U. S. 412, 23 S.Ct. 730 (1903) it was held that although the telegraph company was an agent of the Federal government in performing services for it, as well as for the public generally, the immunity extended only to its relation with that government and did not exempt its property from State taxation. A more recent case along the same lines is that of *Susquehanna Power Co.* v. *Md.*, 283 U.S. 291, 51 S. Ct. 434 (1931). The plaintiff there was a hydro-electric power company acting under a license from the Federal Power

Commission. It erected a dam and power plant, and as part of the project, had acquired lands partly in the river bed and partly on adjoining uplands, which lands were submerged by the water. The court held all the land to be subject to a State tax because in the words of the court, "Where a franchise is granted by the Federal government to a private corporation to effect some governmental purpose, the property owned and used by the grantee in the exercise of the privilege, but for its private business advantage, is subject to state taxation."

When an instrumentality is not engaged primarily in a private business, but is an agency solely engaged in performing strictly governmental functions, than its property is within the rule; this is established in *Clallam County* v. *U. S.*, 263 U. S. 341, 44 S.Ct. 121 (1923), wherein it was held that a State cannot tax the property of a liquidating company, which though performed under her laws, was brought into existence and operated by the United States, whose property was furnished, whose stock and bonds were held, and whose assets realized from liquidation were to be taken over by the United States alone. That the line is rather fine is indivated in *Gromer* v. *Standard Dredging Co.*, supra, wherein a tax which was levied by Porto Rico upon certain of the company's property that acquired a situs within the territory, was upheld although such property was used exclusively by the owner for carrying out a contract with the United States. In this latter case the dredging company stood only in a contractural relations with the Federal government, as compared with complete ownership and control of the liquidating company by the Federal government in the *Clallam County* case.

Though not strictly direct property taxes, the inheritance tax cases seem to fit more accurately in this section; in *U. S.* v. *Perkins*, 163 U. S. 625, 16 S.Ct. 1073 (1896) it was held that such a tax may be levied by a State upon a bequest to the United States, and in *Snyder* v. *Bettman*, 190 U. S. 249, 23 S.Ct. 803 (1903), by the United States upon a bequest to a municipality as a subdivision of the State. The reason which the court gives for its decision in these two cases was that the tax was upon the transmission by will or interstate laws, and attached before the property came into the hands of the municipality or the United States and consequently was not a direct burden upon them.

The second section deals with taxation upon income where the tax is levied for revenue purposes; and this section is subdivided to deal first with income derived from the possession of obligations of the sovereignities, and secondly, with income which is derived from business activity.

In *Pollack* v. *Farmers Loan and Trust Co.*, 157 U. S. 429, 15 S.Ct. 673 (1895) the court held that Congress is without power to levy

a tax upon the income derived from municipal bonds though held by a private enterprise. That the Federal government cannot tax the bonds themselves which were issued by a State or one of its municipal bodies under its authority which were held by a private corporation, was decided in *Mercantile Bank* v. *N. Y.*, 121 U. S. 138, 7 S.Ct., 826 (1887). However, the Federal government can tax the profit which an individual realized from the resale of State and municipal obligations *Willicut* v. *Bunn*, 282 U. S. 216, 51 S.Ct. 125 (1931), but cannot impose a stamp tax upon a bond which a State law requires to be given as a prerequisite to the right to sell liquor within the State. *Ambrosini* v. *U. S.*, 187 U. S. 1, 23 S.Ct. 829 (1902). In *Plummer* v. *Coler*, 178 U. S. 115, 20 S.Ct. 829 (1900) a State inheritance tax is valid although measured by the value of United States bonds transmitted, and in *Greiner* v. *Lewellyn*, 258 U. S. 384, 42 S.Ct. 324 (1924) Congress can tax a transfer by inheritance to the full amount although it includes State and municipal bonds. State laws taxing stockholders at full value, shares in National banks, are upheld although the bank owns tax exempt United States bonds. *Van Allen* v. *Accessors*, 3 Wal. 573, 18 L.E. 229 (1865); *Peoples National Bank* v. *Board of Equalization*, 260 U. S. 702, 43 S.Ct. 98 (1922). So a tax upon deposits was upheld, though such deposits were invested in U. S. securities, *Society for Savings* v. *Coite*, 6 Wal. 594, 18 L.E. 897 (1867), and upon the same principle, a tax lawfully imposed upon the exercise of corporate privileges within the taxing power may be measured by income from the property of the corporation, although a part of such income is derived from non-taxable property. *Flint* v. *Stone-Tracey Co.*, supra. But a tax upon the privilege of doing a corporate business, measured in part by the amount of non-taxable interest received, may be adjudged unconstitutional because of being a tax on such interest, if it be fairly inferable that the real purpose and effect of the tax was to reach specifically these non-taxables rather than being only an incidental burden thereon. *McCallen Co.* v. *Mass.* 279 U. S. 620, 49 S.Ct. 432 (1929).

The next division concerns the tax levied upon income derived from a business activity. A State cannot levy a tax upon the salary of the Captain of a United States revenue cutter, *Dobbins* v. *Commissioners*, 16 Peters 435, 10 L.E. 1022 (1842); nor can the Federal government impose a tax upon the salary of a judicial officer of a State, *Collector* v. *Day*, supra; but the Federal government can tax the income of consulting engineers engaged by a State for work not permanent nor continuous in character on public works, whose duties are prescribed by contract, and who takes no oath of office and are free to accept other

concurrent employment. *Metcalf and Eddy* v. *Mitchell*, supra. Also the Federal government can tax the salary of a manager of a city water works system owned and operated by a city, despite the fact that approximately 40 per cent of the water was used by the city. *Denman* v. *Commissioners*, 73 Fed. (2) 193 (1934). This latter case follows *S. Carolina* v. *United States*, supra, in holding that when a municipality, as part of a State, engages in operating a city water works, it is not engaged in an essential governmental function, and therefore the salaries of its employees are not exempt, since they are not engaged in performing essential governmental functions.

A state cannot impose a tax for the privilege of selling gasoline which is measured by so many cents per gallon of gasoline sold, for the amount sold to the United States Coast Guard Fleet and to a Veterans' Hospital. *Panhandle Oil Co.* v. *Mississippi*, 277 U.S. 218, 48 S.Ct. 451 (1928). Also when a motorcycle is sold by the manufacturer to a municipal corporation of a State for use in its public service, the Federal government cannot levy a tax thereon, although the statute requires the manufacturer to make returns of their sales and to pay the tax. *Indian Motor Cycle Co.* v. *U. S.*, 283 U. S. 570, 51 S.Ct. 601 (1931).

The recent reversal by the Supreme Court on the question of the taxability of income derived from patents and copyrights granted by the Federal government is interesting. *Long* v. *Rockwood*, 277 U. S. 142, 48 S.Ct. 463 (1928) held that such income was subject to taxation by the State of Massachusetts. The decision was criticized severely on the grounds that the property in the patents belonged to individuals, and not to the Federal government, and a non-discriminating tax upon such income would not impair the efficiency of the Federal government in the exercise of its function of protecting science and useful arts. So in *Fox Film Co.* v. *Doyal*, 286 U. S. 123, 52 S.Ct. 546 (1932) the court reversed its position and held such income to be subject to State taxation.

Looking next to the corporations themselves, we find that a State cannot levy a tax upon the operations of a bank organized under a Federal banking act. *McCullough* v. *Md.* supra; *Osborne* v. *U. S.*, 9 Wheat. 738, 6 L.E. 204 (1824). Also a State has no power to impose a tax upon a franchise granted to a corporation by the United States; this was decided in *California* v. *Pacific R. R. Co.*, 127 U. S. 1, 8 S.Ct. 1073 (1888) wherein California attempted to tax the franchise of a railroad company. But a State statute requiring a telegraph company to pay a tax upon its property within the State, valued at such proportion of its capital stock as the length of its line within the State

bears to its total length, deducting a sum equal to the value of its real estate and machinery subject to local taxation, was valid although no deduction was allowed for the value of its franchise from the United States. *Western Union Telegraph Co.* v. *Taggart*, 163 U. S. 1, 16 S.Ct. 1054 (1896).

When the corporation is privately owned and merely contracts with the Federal government, rather than existing under an expressly granted franchise, the corporation is not thereby rendered an essential governmental agency exempt from State taxation. In *Baltimore Shipping Co.* v. *Baltimore*, supra. certain lands held by the United States were conveyed to a private corporation for the construction of a dry dock; it was held that the profits of this corporation were subject to a State tax although the United States had the right to the use forever of the dry dock at any time for repair of her vessels free of charge for dockage, and the land if diverted to any other use would revert to the United States. Likewise a State tax upon premiums paid to a surety company on bonds of United State government officials given by surety company in compliance with a Federal act was upheld. *Fidelity and Deposit Co. of Md.* v. *Penn.*, 240 U. S. 319, 36 S.Ct. 298 (1916). In the more recent case of *Trinity farm* v. *Grosjean*, supra, decided in March, 1934, a corporation entered into a contract with the Federal government to build levees on the Mississippi River; the court held that the corporation was not such a Federal instrumentality as to escape a State tax levied upon the amount of gasoline used in engines employed in the work.

If a State engages directly by its own officers in a business which is of a private nature, that business is not thereby withdrawn from the taxing power of the Federal government. *S. Carolina* v. *U. S.*, supra. The same principle seems to apply if a municipality engages in a business of a private nature as in *Denman* v. *Commissioners of Internal Revenue*, supra, where it was held that a waterworks system owned and operated by a city was not such a State instrumentality as to exempt the salaries of its employees from Federal taxation. Yet where the Federal government leased certain restricted Indian lands to private individuals for the purpose of working the oil and gas found thereon, it was held that the State could not interfere with such leases by imposing an occupation or privilege tax; *Choctaw, O. & Gulf R. R. Co.* v. *Harrison*, 235 U. S. 292, 35 S.Ct. 27 (1914); by taxing such leases; *Indian Territory Illuminating Oil Co.* v. *Okla.*, 240 U. S. 522, 36 S.Ct. 453 (1916); by imposing a tax on the gross value of the production of oil and gas less a royalty interest; *Howard* v. *Okla. Oil Co.*, 247 U. S. 503 (1918); or by a tax upon the net income derived by the lessee from the sale of his

share of gas and oil. *Gillespie* v. *Okla.*, 257 U. S. 501, 42 S.Ct. 171 (1922). The same rule seems to apply when oil and gas leases are executed to private individuals by the State upon portions of public school land. *Coronado Oil Co.* v. *Burnett*, 285 U. S. 393, 52 S.Ct. 443 (1932). But where a municipality makes such a lease, it was held in *Burnett* v. *A. T. Jergins Trust*, 288 U.S. 508, 53 S.Ct. 439 (1933), that the Federal government could levy a tax upon the net income derived by the lessee. It can be seen that this group of cases bears very directly upon the problems before us. These cases will be treated more fully in a later part of the discussion.

It is evident from all these cases that the line which separates the exempt from the non-exempt is not clear and well defined, but on the contrary is vague and uncertain. In the last analysis the question seems one of degree to be devided by the courts in reference to the facts of the situation and in view of their previous decisions.

### B. *The Rule as Applied to the Conducting of Athletic Contests for Fixed Admission by State Colleges and Universities.*

It has become generally recognized that education is one of the functions of government. As stated in 24 R. C. L. 558, "The primary purpose of the maintenance of the common school system is the promotion of the general intelligence of the people constituting the body politic, and thereby to increase the usefulness and efficiency of the citizens in which the government of society depends." The Federal government has not generally entered into the field of education; it has been the States through their constitutions and statutes that have assumed the public education of their own children. This has been so prevalent that one is warranted in concluding that it is an essential governmental function of a State to carry on a system of public education.

But when a State extends its activity beyond the ordinary public schools into the field of higher education in college and universities, is she still engaged in an essential governmental function, or is the State then engaged in a governmental function which is no longer a strictly governmental function?

The cases which have arisen have not completely answered this question. The court in *Marland* v. *U. S.* 53 Fed. (2nd) 907 (1931) makes this statement, "The establishment and maintenance of public schools, State colleges and universities by the State in conformity with its constitution and the enactments of its legislature, is an essential governmental function." Under the facts of the case, however, it does not

seem that the leased land was held by the State for a particular college or university but for school purposes generally. No doubt part of the receipts did go to State universities and colleges, but under the facts of the case the statement seems to be only dictum.

*Group No. 1 Oil Co.* v. *Bass*, 38 Fed. (2nd) 680 (1930) involved lands leased by the State of Texas for the benefit of the University of Texas. The Federal District Court therein held that the maintenance by the State of its university was an essential governmental function, and that the income of the lesee of such land was exempt from Federal taxation. On appeal the Circuit Court of Appeals 41 Fed. (2nd) 484 (1930) reversed this decision and held the income of the lessee to be subject to the Federal tax, but did not decide definitely as to whether or not the State in maintaining the university was engaged in an essential governmental function. The Court, however, did not expressly overrule the decision of the District Court in this respect, but based its decision of reversal on another ground. From this one might infer that the court felt that there was sufficient merit as not to warrant its express overthrowal. The Supreme Court of the United States affirmed the Court of Appeals without comment upon this issue.

In *Coronado Oil Co.* v. *Burnett*, 50 Fed. (2nd) 998 which involved lands leased by the State for the benefit of the common schools, the Court commented upon the *Group No. 1 Oil Co.* case and found that the only substantial difference between that case and the case at bar was the existence of the peculiar property law of Texas in that previous case. The Court did not see any difficulty in holding that a State was engaged in an essential governmental function in maintaining a university. When this case was heard in the Supreme Court, supra, Mr. Justice Stone wrote a dissenting opinion concurred in by Justices Brandeis, Roberts, and Cardozo in which he said in comparing these same two cases, "The leasing by the National government of Indian oil lands in Oklahoma to private lessees for the benefit of the Indians, the leasing by Oklahoma of its school lands in like fashion for the benefit of the schools of the State, are no more and no less governmental enterprises than the leasing by Texas of its oil land for the benefit of the State university." The majority opinion had not made an issue of this particular point.

In the *Board of Trustees of the University of Illinois* v. *U. S.* 289 U.S. 48, 53 S. Ct. 509 (1933) it was held that the University in importing scientific apparatus for use in one of its educational departments was not immune from Federal custom duties. The court said, "It is for Congress to decide to what extent, if at all, the States and

their instrumentalities shall be relieved of the payment of duties on imported articles."

These cases do indicate a tendency toward an acceptance of such being an essential governmental function and from a practical standpoint it seems that such a decision would be the correct one. The reason behind the system of public school education was to promote the general intelligence of the people and to increase the usefulness of those citizens on whom the State must depend. At one time the economic, political, and social conditions of our country may have been understandable, without advanced education. But conditions have changed, and the realization is stronger today than ever before, that the complexity of our civilization demands increased study and specialization in the fields of higher education if we are to intelligently meet the serious problems of today with any degree of success. And this intelligence must not be confined to those individuals who are to be at the helm of government, but such must also be present at the polls, where the attitude of people generally toward the issues of the day is made known. For these reasons it seems that the establishment and maintenance of colleges and universities by the States is an essential governmental function. As an essential governmental function the Federal government cannot, under the rule laid down in *McCullough* v. *Maryland,* supra, tax the instrumentalities, means, and operations by which the State carries out this function.

Another problem now arises. With the rapid development of the general field of education, the activities of such institutions have been extended into many new fields. Many of these activities, although incidental to the performance of the function of education, would seem more likely to be classified as private business enterprises. For example, the students of the agricultural department farm upon university land and market the produce grown thereon; other departments of the university conduct plays, debates, concerts, or athletic contests which are open to the public at fixed admission prices. These activities would be classified as private business enterprises were it not for the fact that they are conducted in connection with the university and its educational program.

As these institutions increase their activities, some will tend to be more remote from a strict educational function. It then becomes necessary to determine whether such activities are exempt from Federal taxation under the immunity of the institution which is an instrumentality of the State in the performance of the governmental function of education.

Here, the State through the athletic department of the university,

is conducting an athletic program which is open to the public at a fixed admission price. Is such activity immune from Federal taxation as being an instrumentality, means, or operation by which the State exercises its essential governmental function of education?

At first glance it would seem that the case of *S. Carolina* v. *U. S.*, supra, would control in this situation, and such activity would be taxable, for where a State carries on a business of a private nature, such business is not withdrawn from the taxing power of the Federal government. The Court foresaw the danger of the States, under the guise of regulation, and with a view to a profit, taking possession in a similar manner of other objects subject to the Federal tax. When there is added to that the growing movement in favor of ownership and operation by the public of so-called public utilities, there is a danger of so curtailing the source of revenue to the Federal government as to seriously hamper it in its operations. The tax was upheld although the business entered into was incidental to the exercise of the governmental function of protecting the public welfare.

However, serious inroads have been made in the holdings of *S. Carolina* v. *U. S.* and of *Helvering* v. *Powers*, supra, in situations dealing with leases made by the Federal government of land held for the benefit of the Indian tribes of the nation, and similar leases made by the State, of land held for the benefit of State educational institutions. The cases bear so directly upon the problem before us that a resumé of these decisions is vital at this point.

The Federal government owned certain lands, valuable because of the natural resources found thereon, for the benefit of the Indian tribes. These lands were leased to private individuals or companies who produced such resources and sold them on the market, the Indians to receive as agreed per centage of the ore, or of the gross income, or net income. The States attempted to tax the gross revenue of the lessee, *Choctaw and Gulf R.R.* v. *Harrison*, supra, the capital stock of corporations acting as lessees, *Indian Oil Co.* v. *Okla.*, supra, the gross production, *Howard* v. *Gipsy Oil Co.*, supra, the net income of the lessee, *Gillespie* v. *Okla.*, supra, and the ores mined and in the bins by an ad valorem tax, *Jaybird Mining Co.* v. *Weir*, 271 U. S. 603 (1926); but every attempt was ruled out as unconstitutional. The Court found in each of the cases that the agreement with the Indians imposed upon the United States the duty of exploiting the resources upon the lands, and that the lessees were the instrumentalities through which that obligation was being carried into effect.

Similarly, the States held certain lands for the benefit of their edu-

cational institutions which they leased to private individuals. The two leading Supreme Court cases involving such leases are *Group No. 1 Oil Co.* v. *Bass*, 283 U. S. 279, 51 S. Ct. 432 (1931) and *Coronado Oil Co.* v. *Burnett*, supra. In the *Group No. 1 Oil Co.* case the state of Texas leased certain land, held by the State for the benefit of the University of Texas, to a private company to produce the oil reserves thereon. A Federal tax levied upon the profits of the lessee after first deducting the State's royalties was upheld. In the *Coronado* case, however, where land held by the State of Oklahoma for the support of cer tain common schools was leased to a private company with the State reserving a part of the gross production, a Federal tax levied upon the income from the lease by the lessee was declared unconstitutional. The decision in the *Group No. 1 Oil Co.* case was principally based upon a settled property rule in Texas which declares that such a lease passes title completely out of the State as a present sale; and the property being no longer that of the State, but of the lessee, the latter could not claim the immunity of the State. The *Coronado* case in commenting upon the *Group No. 1 Oil Co.* case noted this peculiarity of the Texas law in this respect. In following *Gillespie* v. *Oklahoma* the Court brought the school lease cases in line with the Indian lease cases.

The distinction made between the *Coronado Oil Co.* case and the *Group No. 1 Oil Co.* case has been severely criticized as being without any foundation. The distinction seems extremely narrow if it exists at all. During the term of the lease the benefit to the State is as far removed from the State as when the property is conveyed in fee. On the other hand the burden is as substantial upon the State in its receipt of income whether it be of rent when a lease is concerned, or of the royalties when the fee simple is passed. The decision of the *Group No. 1 Oil Co.* case indicates that the Court is seeking to avoid any extension of the Gillespie case. Under this ruling large private incomes are escaping Federal and State taxation, where as to tax these same incomes would be to burden the State or Federal government only remotely and indirectly if at all, since the tax is upon the lessee's share of income or raw material after the State has received its agreed proportion. This would seem to be a wholesome limitation on these lease cases, since it does not effect directly the share which would go to the State or Federal government. For another limitation of the Gillespie case see *Indian Co.* v. *Board of Equalization*, 288 U.S. 325, 53 S.Ct. 388 (1933).

The case of *Burnett* v. *A. T. Jergins Trust*, supra, is very interesting. There the City of Long Beach, California, leased to a private company certain oil lands owned by the city which had previously been

used for her water supply. Under the lease the oil and gas were sold by the parties jointly and the proceeds were divided in agreed proportions between them. The court upheld a Federal tax upon the receipts of the lessee. The lessee relied upon *Gillespie* v. *Okla.* and the *Coronado* case; the court said in commenting upon these cases, "In both of these cases the sovereign was acting as trustee of an express trust with regard to the land leased. In both the burden upon the public use was more definite and direct than in the present case."

It seems then that when a municipality, which is a subdivision of a state, makes identical leases, the activity of such lessees is subject to Federal taxation. But had the State made a lease to the same private company of land which she held for the benefit of her educational institutions, then the business of such lessee would be exempt from Federal taxation as being an instrumentality by which the State exercised an essential governmental function. As said in *Burnett* v. *Coronado Oil Co.*, "When Oklahoma undertook to lease her public lands for the benefit of the public schools she exercised a function strictly governmental in character. Consequently *S. Carolina* v. *U. S.*, much relied upon, does not apply."

The State then in the interest of her educational institutions can exploit the natural resources of her school land through private lessees, and in so doing, such business is immune from Federal taxation, although it be of a private nature, because it is an instrumentality by which the State exercises the governmental function of educating its people. It would follow that the State could operate the same land for the benefit of such institutions through her own officers, since that would merely change the instrumentality by which the governmental function would be performed.

If a State then, in the interest of her educational institution, constructs upon school property a stadium, and with the students of such institution as participants, conducts athletic contests thereon for which she charges admission, is such activity immune from Federal taxation? Is not the reasoning of these school land lease cases applicable to the very problem before us?

The primary interest in both cases is to benefit the educational institution. In both there is a development of the State's educational land for the purpose of deriving revenue therefrom to carry on her educational program which is an essential governmental function; for if education is such a function of the State, *Marland* v. *U. S.*, supra, the State's duty to raise revenue to carry on that function is necessarily implied therefrom.

The development of the land in so far as actual details are concerned is admittedly different, yet fundamentally there does not seem to be any great difference. Should not the State employ the property which she holds for the benefit of her schools in such a manner as will result in the maximum of benefit to such institutions? If there are valuable mineral resources thereon, the State can exploit such resources, and in so doing, that activity whether carried on by officers of the State or private lessees, is immune from Federal taxation. The land, however, may not be valuable for natural resources so the State through the athletic department of the university builds a stadium and conducts athletic contests therein, for which they charge admission. Instead of the private lessee there is the athletic department; instead of constructing on such lands oil wells and other apparatus necessary to produce the oil, there is built a stadium; instead of the natural resources there are the students of the institution. On one hand there is the private business of producing and selling the natural resources, while on the other there is the private business of carrying on public entertainment. Yet in both there is the exercise of the governmental function of deriving a revenue by developing the State's educational land in order that the State could carry on her educational program. It seems that the activity relative to the conducting of such athletic contests for fixed admissions, should be exempt from Federal taxation in the same manner and for the same reason as the activity in relation to the exploitation of the natural resources on educational land for the benefit of the State's educational institutions.

One argument made is to the effect that the proceeds derived from the admissions are not applied by the university for the benefit of general educational purposes, but are disbursed by the athletic department as such department sees fit. Admitting this to be true, it does not follow that the funds are not applied to the benefit of the university. An examination in specific detail of the athletic department noticing its control, operation, and personnel discloses that this argument is of no force.[3]

[3] The physical education plant, with the exception of the gymnasium and the amount privately donated for the stadium, has been constructed by means of the funds derived from receipts from the athletic contests. The title to this athletic plant is in the university. Besides constructing the stadium and natatorium, the department has purchased a site for a university golf course which is to be maintained for the students.

The coaching staff has faculty ranking. Besides conducting their specific sport, they also conduct classes in physical education.

The disbursements and the general policies of the department are under the control of the Athletic Board. This board is composed of eleven men of whom six are appointed by the President of the University, two by the Student Senate, and two are elected from the alumni. Through control of majority vote the policies of the department are decided by the seven men appointed by the President and the Board of Trustees. The Board of Trustees could, if they desired, cause the entire proceeds derived from the athletic contest to be turned into the general university fund to be disbursed for general educational pur-

Another argument is made that the tax is not upon the athletic department but only upon those individuals who buy the tickets; that the burden therefore is upon those individuals, and not upon the athletic department. If not a burden upon the department, it would then be immaterial as to whether the department was or was not an instrumentality of the State in carrying out an essential governmental function.

Since the student tickets go free of any tax, the tax is not upon the gross receipts but upon the individual admission. The University fixes its price for the seat, and the additional tax is borne by the purchaser to be collected by the University for the Federal government.

Actually, however, the gate receipts are curtailed by such a tax. The department has the alternative of adding the tax to the existing admission price and suffering from a consequent dropping off in attendance, which normally results from increased prices of admissions, or keeping the price intact and receiving a lesser amount from each ticket sold. To this extent it is a burden on the department.

*U. S.* v. *King County*, 281 Fed. 686 (1922) involves a similar situation. There the Federal government attempted to tax tickets for transportation on a ferry operated by a county under State laws. The court said "It is true that in the present case the tax was not imposed directly upon the county but upon the person paying the transportation charges; but it is obvious that the collection of those charges is at least one of the means to which the county must resort to for the purpose of paying the cost of the ferry, which, if insufficient, must be made good from the other revenue or by Federal taxation. Hence it seems plain that the Federal tax here involved is an interference with and a burden upon the governmental functions of the state."

Furthermore, the Federal tax could be increased to such an extent as to render the price absolutely prohibitive; although this is not probable, it would be possible. The decision of Chief Justice Marshall in *McCullough* v. *Maryland* hinges on this very argument. The tax is unquestionably a burden on the department, and not a burden exclusively upon the individual who purchases the ticket.

It was noted previously that *Gillespie* v. *Oklahoma* has been criticized because under its ruling vast private incomes were being given immunity from State and Federal taxation. The situation under discus-

poses. The stadium at the present time houses some two hundred young men under a cooperative dormitory plan, thereby making it possible for these men to attend the University who otherwise would be unable to do so because of a lack of financial means. This work is under the supervision of the University Examiner.

From these facts we see that the Athletic Department is so related to the physical education program and to the University in general as to be an essential part thereof. The proceeds of the contests are applied to the benefit of the University.

sion is not subject to this criticism, because the entire income accrues to the athletic department to be used for the benefit of the University. There is lacking that element of a purely private enterprise operated for the private gain which accrued to the lessees over and above that amount which went to the State or Federal government in the Indian lease cases and the school land lease cases.

The maintenance of a university by a State is an essential governmental function. The means, instrumentalities and operations by which she carries out this function are therefore immune from Federal taxation. The carrying on of athletic contests through the athletic department of the university on school land for the purpose of deriving a revenue to be applied to the benefit of the university is a means by which the State carries out this essential function of education. As such a means the activity thereof is immune from taxation. The tax here is a burden on the means by which the State carries out her function of education, and is therefore unconstitutional.

This seems the logical conclusion from the decisions rendered by the Supreme Court of the United States. The decisions of this Court cannot be predicted with certainty in advance, but it seems that if the Court is to come to any other conclusion it must necessarily overrule a long line of cases dealing with leases made by the Federal government of land held for the benefit of the Indian tribe and leases of land held by the State for the benefit of her schools. Also the result is desirable since the entire proceeds inure to the benefit of the university without the intervention of any private enterprise for a profit, which profit is escaping Federal or State taxation, an element which has caused the holding of *Gillespie* v. *Oklahoma*, supra, to be severely criticized.

## II. The Tax as Imposing Duties on State Officers and Employees.

The Act imposes upon the Athletic Department the duty of collecting the amount thereof from the person making the payment, of keeping certain prescribed records, of making certain returns under oath, and of paying in the money so collected when due. It unquestionably subjects the department to considerable additional work and expense. Can these duties be constitutionally imposed upon the Department?

In general the State and Federal governments act independently of each other in carrying out their executive and administrative functions, and the principle has become established that the Federal government cannot impose upon officers of the State the imperative duties of execut-

ing Federal laws, nor can the State impose similar duties upon Federal officers. *Kentucky* v. *Dennison*, 24 How. 66, 16 L.E. 717 (1860). However, there seems to be no constitutional objection to the granting of such powers by one sovereign to the officers of the co-sovereign, if the officers are willing to carry out such duty and their sovereign does not expressly prohibit such act. It was held in *Prigg* v. *Penna.*, 16 Pet. 539, 10 L.E. 1060 (1842) that in the absence of express prohibition by the State, the State is presumed to give its consent to the exercise of Federal functions.

The members of the Athletic Board cannot be classified as officers of the State. This is a conclusion drawn from *State* v. *Hewitt*, 3 S.D. 187, 52 N.W. 875 (1892) wherein it was held that the trustee of a State agricultural college appointed by the Board of Regents of Education was not a "State Officer" within the meaning of the term. They are, however, employees of the State, and the question arises as to whether or not these same rules apply to State employees. It is necessary then to find the reason behind the rule.

*Kentucky* v. *Dennison*, supra, is the only case where an officer of the State has refused to carry out a duty imposed upon him by the Federal government to execute Federal laws. In other instances the duties have been performed by State officers and acquiesced to by the State. Thus it has been upheld that State magistrates can, by act of Congress, be authorized to arrest fugitive slaves, *Prigg* v. *Penn.*, supra; that congress can authorize State justices of the peace to issue warrants for the arrest of deserting seamen, *Robertson* v. *Baldwin*, 165 U. S. 275, 17 S. Ct. 326 (1897); that State officials can be used by the Federal government in the exercise by the latter of the power of eminent domain, *U. S.* v. *Jones*, 109 U. S. 513, 3 S. Ct. 346 (1883); that the United States can make use of State courts in the granting of naturalization to aliens, *Holmgren* v. *U. S.*, 217 U.S. 509, 30 S. Ct. 588 (1910); and that the United States may avail itself of the use of State officials for the execution of its Selective Draft Laws during war time, *Arver* v. *U. S.* 245 U.S. 366, 38 S. Ct. 159 (1918).

In the Selective Draft cases the State officers were performing the duties imposed upon them with the consent of the States. The complainants were citizens of the State who claimed the Draft Laws to be unconstitutional because of imposing duties upon officers of the State. The court said "We are of the opinion that the contention that the act is void is a delegation of Federal power to State officials because of some of its administrative features is too wanting in merit to require further notice."

In *Kentucky* v. *Dennison* the opinion reads, "And we think it clear that the Federal government, under the Constitution, has no power to impose on a State officer as such, any duty whatever, and compel him to perform it; for if it possessed the power, it might overload the officer with duties which would fill up all his time, and disable him from performing his obligations to the State, and might impose upon him duties of a character incompatible with the rank and dignity to which he was elevated by the State."

The former of these two reasons might be extended to cover employees of the State as well as officers of the State. The employees have certain duties which they perform for the State, and to impose Federal duties upon them would disable them to that extent from performing their duties for the State.

On the other hand, the courts may hold the ruling of *Kentucky* v. *Dennison* strictly to the facts of that case. It is pointed out in 22 R.C.L. 381 that "an officer is distinguishable from an employee in the greater importance, dignity, and independence of his position in being required to take an official oath and perhaps to give an official bond, in the more enduring tenure, and in the fact that the duties of the position are prescribed by law. Furthermore, a mere employee does not have the duties or responsibilities of a public officer." The fact that the duties of an employee are not prescribed by law and the tenure of office not fixed make an imposition of Federal duties upon him less onerous to the State than in the imposition of such duties upon a State officer. It may be that this difference in the degree of the burden upon the State when an employee of the State is concerned, as compared with the burden when an officer of the State is concerned, will cause the courts as a matter of practicability, to allow the Federal government in the execution of its powers to impose certain duties upon employees of the State.

An examination of the duties imposed upon the Athletic Department indicate that they are not so burdensome as to effect it in any substantial manner in its function of deriving revenues for the benefit of the university. These duties consist, for the most part, of making certain bookkeeping entries and keeping specified records, and can be coordinated into the general operations of the Department without great difficulty.

It is difficult to predict which of these two approaches the Court will adopt, and the rule as laid down in *Kentucky* v. *Dennison*, supra, does not lend a great deal of assistance in determining beforehand what their decision will be. One is impressed by the rarity of dissent on the part of the State, its officers, and employees despite the rather frequent

use by the Federal government of these same officers and employees. With but one exception the States have not seen fit to prohibit the deligated duties, nor have the officers seen fit to refuse to perform the same.

Until the State, through its legislature, prohibits the performance of these duties, or the Athletic Department refuses to perform them, the constitutionality of the act in this respect will not be questioned. In the event of a decree, there will be no relation back, and such decree will be effective only from the time of the legislative prohibition or the express refusal by the Department.